October 2, 2003

Solution Must Be Affordable and Permanent

Enacting Meaningful Asbestos Reform

Executive Summary

- The explosion of asbestos-related litigation is bankrupting scores of companies and destroying jobs while failing to provide proper compensation to those actually injured by asbestos exposure.
  - At least 600,000 claimants have sued more than 8,400 defendant companies alleging some kind of injury caused by asbestos exposure.
  - Less than 45 percent of all asbestos litigation expenditures end up in the hands of plaintiffs, and 90 percent of plaintiffs are not impaired in any way.
  - The 67 companies bankrupted by asbestos litigation have facilities in every State except Rhode Island, Hawaii, and North Dakota. These bankruptcies have destroyed 60,000 jobs so far.
- The Judiciary Committee has reported a bill that creates a federally-administered trust fund to reach these goals, but Democrat-sponsored amendments at the markup resulted in a bill that many believe is too costly and open-ended. The final bill should be improved.
  - Reform should provide a truly permanent solution to the crisis.
  - Reform should have a reasonable cost that ensures that those who are truly sick due to asbestos get fair compensation.
  - The federal taxpayer should never be forced to bail out private industry for the asbestos litigation explosion.

Introduction

Lawsuits alleging injuries caused by asbestos exposure are bankrupting companies, costing tens of thousands of jobs, and creating a drag on economic recovery. Meanwhile, the asbestos victims who are most sick and in need of relief are receiving paltry sums as the bulk of compensation goes to trial lawyers and plaintiffs who suffer no immediate injury or impairment. Our civil justice system is failing asbestos victims, it is failing defendants, and it is failing our economy. Reform is long overdue.

Earlier this year, the Judiciary Committee began to move a legislative proposal to create a trust fund made up of contributions from defendants and their insurers. The initial bill as proposed by Chairman Hatch was the result of months of difficult negotiation among the stakeholders most affected by this litigation: defendant companies, their insurers, labor unions, and the asbestos trial bar. The end product of these negotiations was already the result of significant compromise, and represented the Senate's best chance to enact meaningful reform.

Chairman Hatch introduced and moved S. 1125 as a compromise measure, but as the committee markup progressed, onerous amendments pushed by Democrats in the Judiciary Committee resulted in a dramatically different bill. (Yet despite these amendments, only one Democrat supported the committee's marked-up bill.) That marked-up bill now on the Senate Calendar is too costly, too open-ended, and too likely to collapse and force this crisis onto the congressional agenda again in a few years. The Senate should work to improve the bill to eliminate some of the harsh amendments accepted during markup, and move the bill closer to the compromise that S. 1125 represented when introduced.

Asbestos Litigation is Out of Control

Asbestos-related lawsuits have skyrocketed over the past decades and show no sign of abating. At least 600,000 claimants have sued more than 8,400 defendant companies alleging some kind of injury caused by asbestos exposure — up from "only" 300 defendant companies in 1983.[1] Most defendants are not asbestos sellers or manufacturers but are, instead, companies that have but a tangential relationship to the product. "Nontraditional" defendants include companies from nearly every part of our economy — 75 of the 83 industrial sectors defined by the Commerce Department, including such peripheral industries as financial services, hotels, telecommunications, and even food and beverage.[2] The RAND Corp. estimates that nontraditional defendants are targets of nearly half of all new asbestos claims,[3] and that the litigation "has spread to touch almost every type of economic activity in the United States."[4]

The asbestos litigation explosion has devastated industries and forced many companies into bankruptcy. At least 67 firms have filed bankruptcy due in significant part to asbestos litigation, including at least 35 companies since 1998.[5] Joseph Stiglitz, Nobel Prize winner in economics, estimates that these bankruptcies have destroyed approximately 60,000 jobs so far, and that each of these dislocated workers suffered raw financial losses of up to $50,000.[6] The costs of asbestos litigation overall has already prevented more than 125,000 other jobs from being created, and RAND further predicts that as many as 285,000 additional jobs will *not* be created if the current asbestos litigation system continues.[7] And just as nearly every industrial

[1] RAND Institute for Civil Justice, "Asbestos Litigation Costs and Compensation" (2002), p. 49, available at http://www.rand.org/publications/DB/DB397/.

[2] Joseph Stiglitz et al., "The Impact of Asbestos Liabilities on Workers in Bankrupt Firms" (2002), pp. 19-20, available at http://www.asbestossolution.org/stiglitz_report.pdf. Dr. Stiglitz is the co-winner of the 2001 Nobel Prize in Economics, and has served as the World Bank's Chief Economist and the Chairman of the President's Council of Economic Advisers.

[3] RAND, p. 47.

[4] RAND, p. vii.

[5] RAND (data updates from January 2003; on file at the Senate Republican Policy Committee).

[6] Stiglitz, p. 26, 43.

[7] RAND, p. 74.

sector has been impacted, so too has nearly every State: these bankrupt companies had facilities in every State except Rhode Island, North Dakota, and Hawaii.[8]

The harm to the economy has not been justified by any confidence that workers who were genuinely injured and impaired by asbestos exposure were receiving appropriate compensation. However, our civil litigation system is failing true victims just as dramatically as it is destroying jobs and wealth. Approximately $54 billion has been spent so far on asbestos litigation, but the majority of that money is not going to injured parties.[9] Especially because of the prevalence of fraud and suits by the unimpaired,[10] and because plaintiffs' attorneys have made claims that would lead to bankruptcy, defendant companies usually vigorously defend against these lawsuits. Thus, defendants' expenses (mostly lawyers) amount to approximately 25 percent of total litigation costs thus far, while plaintiffs' expenses amount to around 30 percent, leaving less than 45 percent of total asbestos-related litigation expenditures to be divided up among the actual plaintiffs.[11] Moreover, substantial evidence detailed in the Committee Report accompanying S. 1125 demonstrates that some plaintiffs' attorneys have been defrauding defendants and the justice system by encouraging plaintiffs to lie and submitting trumped-up claims of injury and impairment.[12]

Thus, not only have the courts been burdened by the sheer volume of cases — legitimate and fraudulent alike — but also they have been unable to ensure that even a majority of asbestos compensation goes to plaintiffs who are actually impaired. The vast majority of new claims — approximately 90 percent —are made by people who do *not* have any sort of cancer or mesothelioma (a type of cancer known to be caused by asbestos exposure).[13] Indeed, most of these claims are not even by people who are impaired in any way. As the RAND report concluded, "a large and growing proportion of the claims entering the system in recent years were submitted by individuals who have not incurred an injury that affects their ability to perform activities of daily living." The court system has failed to sort out these claims by the unimpaired, so that roughly 65 percent of total dollars paid to plaintiffs have gone to persons *without* malignant diseases of any sort.[14] This lack of reasonable prioritization is exacerbated by the unacceptable delays that all asbestos plaintiffs face in the courts — a delay twice the rate of non-asbestos cases.[15] Our civil justice system is ill-equipped to handle this volume of cases, especially when problems are compounded by attorney-driven fraud and manipulation.

Support For Reform is Broad

If there is any doubt that the court system is failing plaintiffs and defendants alike, one need only listen to the pleas for help coming from the judges themselves. The Supreme Court has three times called on Congress to provide a national solution to this problem.[16] A special

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[8] Stiglitz, p. 21.
[9] RAND, p. vii.
[10] See Committee Report 108-118, Additional View of Senator Kyl, pp. 84-98.
[11] RAND, p. 60.
[12] See Committee Report 108-118, Additional View of Senator Kyl, pp. 84-98.
[13] RAND, p. 46.
[14] RAND, p. 65 (citing data from Tillinghast-Perrin and Claims Resolution Management Corp.).
[15] *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 631 (1997) (Breyer, J., concurring).
[16] See *Amchem Products, Inc. v. Windsor*, 521 U.S. 591, 628-629 (1997); *Ortiz v. Fibreboard Corp.*, 527 U.S. 815, 821 (1999); *Norfolk & Western Rwy. Co. v. Ayers*, __ U.S. __, 123 S. Ct. 1210, 1228 (2003).

committee of the U.S. Judicial Conference (appointed by Chief Justice Rehnquist) concluded as far back as 1991 that only congressional action could prevent all "resources for compensation" from being exhausted, thus leaving "thousands of severely damaged Americans with no recourse at all."[17]

The courts' exasperation with the current morass is shared by defendants and their insurers, virtually all of whom have asked Congress to craft a comprehensive solution. These requests have been echoed by many labor leaders who recognize that bankrupt companies employ far fewer workers than healthy ones, and who have seen injured union workers receive pittances when making claims against bankruptcy trusts set up to pay asbestos claims. Even some trial lawyers — in particular those attorneys who represent the truly injured and impaired (a small minority of current claimants) — have called for reform to prevent the exposed-but-unimpaired from continuing to milk defendant funds at the expense of their genuinely harmed clients who suffer from mesothelioma or lung cancer caused by asbestos exposure.

As the *Wall Street Journal* editorialized at the beginning of this Congress, "If the opportunity is missed now, there's hardly a company in the Fortune 500 not at risk."[18]

Understanding the FAIR Act as Reported from Committee

The Senate Judiciary Committee earlier this year responded to these calls for a national, comprehensive solution by holding hearings, marking up, and reporting out S. 1125, the Fairness in Asbestos Injury Resolution Act of 2003 (the "FAIR Act"). When originally introduced by Chairman Hatch, S. 1125 represented a compromise — the result of months of negotiations between the defendant, insurer, labor, and trial lawyer communities — and was the best opportunity Congress has had to address this crisis. The solution — a trust fund made up of private funds — could prove effective, but only if costs were contained and it represented a truly permanent end to litigation.

However, as the committee held hearings and marked up the bill, some stakeholders saw opportunities to destroy consensus and harm the ability of Congress to pass a bill at all. Democrat-sponsored amendments destroyed finality — *a precondition to any trust fund* — and increased compensation amounts to unrealistic levels, especially for those who are either not injured or not impaired by asbestos exposure. And despite the adoption of these Democrat-sponsored amendments, only one Democrat voted for the bill, and she has offered no guarantee that she will support it on the floor.

S. 1125, which was already the result of compromise when introduced, still provides the basic structure for meaningful reform — reform that will provide adequate compensation to the truly injured and impaired; a reasonable cost that does not bankrupt viable businesses; and finality to the crisis. But it is up to the Senate to restore the hope for a national solution that the introduction of S. 1125 represented by solving the problems that Democrat-sponsored amendments in committee created.

[17] Report of the Judicial Conference Ad Hoc Committee on Asbestos Litigation (March 1991), pp. 3, 27-35.
[18] Editorial, "Containing the Asbestos Blob," *Wall St. Journal* (Jan. 16, 2003).

Summary of the FAIR Act as Reported from Committee

The FAIR Act would establish a privately-funded trust fund made up primarily of mandatory contributions from current defendants and their insurers. Plaintiffs who believe they have been injured by asbestos exposure would submit claims to the administrator of the trust fund with evidence that they were exposed to asbestos for a sufficient period of time to cause their asbestos-related medical condition. Qualified claimants would be paid a fixed amount depending on eligibility and disease type. The trust fund approach eliminates the litigation process and the tens of billions of dollars currently being spent on attorney fees. Properly administered, the trust fund should ensure that nearly all defendants' and insurers' asbestos expenditures end up in the hands of injured claimants. And by paying fixed award amounts depending on pre-set eligibility criteria, the FAIR Act would ensure that the truly impaired are compensated.

Funding the Trust Fund: Who Pays, and How?

The proposed trust fund would be comprised of money from three sources: the funds remaining in asbestos trusts created by companies that were bankrupted by asbestos litigation; mandatory annual contributions from defendant companies that have past liabilities; and mandatory annual contributions from those defendants' insurers. The FAIR Act also would provide for additional contributions from defendants and insurers if necessary to meet claims. Total contributions, detailed below, would amount to between $108 billion and $139 billion.

The funds in existing bankruptcy trusts allocated for asbestos claimants amount to roughly $4 billion. These trusts were created when past defendants went bankrupt despite having outstanding asbestos liabilities. Because of claims by the unimpaired, the typical asbestos trust pays pennies on the dollar as compared to what was intended when the trusts were created. The FAIR Act would shift all these monies into the main trust fund.

Mandatory contributions would make up most of the fund. The FAIR Act would compel defendant companies and their insurers to make annual contributions into the trust fund over a 27-year period, for a total collective contribution of $104 billion. The bill would divide these payments equally between the defendant companies and the insurers — $52 billion each. Initial annual payments would be highest (an estimated $5 billion for each group), but would decline over the 27 years on a set schedule.

Allocation within each group (defendants and insurers) is also governed by the bill. The bill would allocate payment obligations among defendant companies based on their past asbestos litigation-related exposure, so a company that has a track record of substantial expense is presumed to have greater future liabilities and, therefore, would be compelled to pay more into the fund. Small businesses are exempted from payment altogether. On the insurer side, allocations among insurers would be determined by a special commission created by the FAIR Act that would determine proportionate obligations depending on premiums received, losses paid, reserve levels, and projected future liabilities.

The bankruptcy trust funds ($4 billion) and the mandatory annual defendant/insurer contributions ($104 billion) would be the only automatic payments into the trust, but the FAIR Act also contains other mechanisms to ensure full funding for claims. The main vehicle for

additional monies is the "contingent call" option, whereby the fund administrator could increase contributions from insurers and defendants if necessary to keep the fund solvent. (Mechanically, the administrator would suspend the defendant/insurers' anticipated declines in mandatory payment amounts on a year-to-year basis.) Through this mechanism, the fund administrator could increase funding from insurers and defendants by as much as $31 billion. The bill also would protect against default by defendant or insurer contributors by requiring all contributors essentially to insure against nonpayment of fellow contributors via a surcharge paid each year. Finally, the Act enables the fund administrator to extend the life of the fund after 27 years if necessary to meet obligations — thus requiring even more money from insurers and defendants.

The Claims Process: Getting the Compensation to the Injured

The trust fund concept embodied in the FAIR Act aims to provide a no-fault process that drastically cuts transaction costs and delivers compensation to the injured and impaired faster than would the tort system. To that end, persons believing they are injured by asbestos must submit claims through a special master (or administrator) who works under the authority of the Court of Federal Claims. Claimants must include their medical diagnoses, their work history, an explanation of their asbestos exposure, a history of their tobacco use, and information regarding prior claims and recoveries. The administrator would review that information and place the claimant in a pre-set category defined in the Act depending on medical, diagnostic, latency, and exposure criteria. If the claimant disagreed with the administrator's categorization of his claim, he could pursue administrative and judicial appeals.

The crux of the claims process is the determination of which category each claimant falls into. By dividing up claimants based on the kind of disease, the level of exposure, and the other eligibility and latency requirements, the FAIR Act provides a structure for ensuring that the largest compensation awards go to those with the most serious injuries that most likely were caused by asbestos exposure. Thus, with a mesothelioma victim — the one malignant disease where asbestos exposure is the only known cause — an eligible claimant would receive $1 million, as could non-smokers who suffer from lung cancer due to asbestos exposure. (Many mesothelioma sufferers today receive less than $40,000 from the current system.[19]) As the severity of the disease decreases and the likelihood that asbestos did *not* cause the disease increases, the award amount declines. For example, those suffering from "other cancers," for which the relationship with asbestos is not established,[20] will still receive $150,000 if they submit medical and eligibility evidence. Lower-level injuries in which claimants suffer no impairment whatsoever may still claim $20,000. And an entire class of unimpaired claimants can obtain lifelong reimbursement for medical monitoring if they can show sufficient exposure.

The claims process is designed to ensure that compensation goes to those most severely injured by asbestos. To that end, the FAIR Act contains another tool designed to protect sufficient funds for claimants with mesothelioma, severe asbestosis, and lung cancer caused by

[19] Prof. Michelle J. White, *Why the Asbestos Genie Won't Stay in the Bankruptcy Bottle*, 70 U. CIN. L. REV. 1319, 1324 n. 25 (2002) (reporting actual claim payments from several "recent" bankruptcy trusts where mesothelioma victims received anywhere from $925 to $40,000); see also Prof. Michelle J. White, "The Hatch Asbestos Trust," *National Review Online* (July 22, 2003) ("The average asbestos plaintiff whose claim was tried in court over the past 15 years received a damage award of just over $1 million in current dollars, but the average claimant whose suit was settled out of court received only about $5,600.").

[20] Committee Report 108-118, Additional View of Senator Kyl, pp. 102-103.

asbestos: a "lockbox" provision. The bill enables the administrator to set aside sufficient funds in any given year to ensure that these most serious injuries are paid *first*, so that claims based on the lesser disease levels do not drain the fund. This provision is crucial to protecting the fund against "exposure only" claimants with no impairment.

The FAIR Act Should Be Improved Before Receiving a Floor Vote

The Judiciary Committee worked with the major interest groups to create a bill that provides a structure for reform. Several meetings and markups resulted in many changes to this bill, but some of those changes require adjustment or reversal before the bill should be passed.

The Biden "Sunset" Amendment

During the closing moments of the last of the markups, the Judiciary Committee adopted the Biden "sunset" Amendment by a vote of 14-5. Under this amendment, the trust fund would shut down permanently if the administrator cannot certify that 95 percent of claim obligations owed in a given year can be paid from funds in the trust. In that event, all claims would return to the tort system and the FAIR Act would become a nullity. As a result, defendants and insurers could pay literally billions of dollars into the fund for several years without any assurance that they were freeing themselves of bankrupting litigation expenses in the future. And if the asbestos plaintiffs bar[21] were to coordinate efforts and cause claimants to swamp the fund in a single year — thus triggering the Biden Amendment — they could wholly undo Congress's efforts.

Because this provision destroys any confidence that the FAIR Act could be a permanent solution, many strongly pro-reform interests — in particular, many insurance companies — seriously question whether the FAIR Act would be an improvement over the current system. The need for a *permanent* solution has always been a driving force behind reform. Without that finality, defendants and insurers alike have great difficulties planning for asbestos liabilities and setting aside funds to pay for litigation. The surprising increase in "exposure only" claims over the past 10 years — driven in large part by manipulation by some lawyers[22] — in particular has raised questions about how many new claimants will come out of the woodwork in the future. Any asbestos reform that fails to eliminate this uncertainty will depress the investment incentives in the defendant and insurer sectors, and will deprive the economy of the jobs and social wealth that a stable economic environment produces.[23] Congress will not be solving the asbestos litigation process if it enacts reform that does not provide the needed finality, which means the Biden "sunset" amendment must come out of the bill.

[21] Anyone doubting the wiliness and unscrupulousness of some members of the asbestos bar should review the exhibits to the Committee Report discussed at pp. 84-98.

[22] See Prepared Statement of Steven Kazan, Esq., Hearing on Asbestos Litigation Before the Senate Judiciary Committee, September 25, 2002, pp. 20-24, in which Mr. Kazan, an asbestos plaintiffs lawyer himself, discusses the attorney-doctor collusion that has driven up false claims. See also Committee Report 108-118, Additional View of Senator Kyl, pp. 84-98.

[23] RAND, pp. 73-74.

Ensuring Solvency for Contributors and the Fund — Curbing Excessive Awards

The FAIR Act as originally proposed included fair and reasonable awards for injuries, especially for those categories where claimants have suffered impairment and where the medical evidence supports a connection between the injury claimed and asbestos exposure. After amendment in committee, awards are even more generous. For example, the FAIR Act now provides an award of $150,000 to persons who in all likelihood have *not* been injured by asbestos exposure — persons suffering from colo-rectal cancers and "other cancers" for which the medical evidence of causation is weak to non-existent.[24] Under the reported bill, even the most worthy claimants (mesothelioma victims) would receive much higher awards than they would receive if they made their claims through an existing bankruptcy trust.[25] The award amounts — increased by amendment during the committee markup process — gained at most one Democrat vote for the bill. They should be curbed prior to final passage on the floor.

Unfortunately, the Senate can expect opponents of this bill to attempt to dramatically *increase* awards. In his minority views, Senator Leahy argued for an increase of 25 percent to 40 percent for awards on lower-level diseases, and suggested that the awards for the dubious "other cancer" diseases, plus the severe lung cancer and mesothelioma impairments, were too low also.[26] Lost in these complaints, however, is any comparison to the real-world values of these claims without the FAIR Act's comprehensive reform,[27] and any genuine effort to explain how these higher awards would be funded without bankrupting the very companies relied upon to pay into the trust fund.

The Senate should reject these efforts to increase the award amounts; indeed, it should scale them back. Failure to roll back the excessive award values provided in the reported bill can be expected to lead some insurers and defendant companies to declare bankruptcy rather than participate in the trust fund. This is because excessive award values will create permanent expectations of payment that will guarantee that the contingent-call provision of the fund will be exercised — thus pushing the total mandatory contributions up to $135 billion. Especially with the Biden amendment's elimination of any guarantee of permanence, companies cannot be expected to survive with these elevated burdens. It should go without saying that bankruptcies harm local communities, while also depriving the economy of the ongoing revenue that is the source of all the trust fund's contributions. Asbestos claimants are not served by a fund that cannot be funded due to increased bankruptcies.

Guarding Against a Taxpayer-Funded Bailout

The elephant in the room throughout the asbestos reform legislative process has been whether the federal government should contribute taxpayer dollars into the trust fund. It should not, and the FAIR Act provides no taxpayer money for the fund. However, it is important to recognize that while defendant companies, insurers, many labor unions, and even some trial lawyers all want a comprehensive national solution, federal contributions are ultimately in all of

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[24] See medical evidence discussed at pp. 102-103 of the Committee Report.

[25] White, 70 U. CIN. L. REV. at 1324 n. 25.

[26] Committee Report 108-118, Minority Views of Senator Leahy et al., pp. 202-205.

[27] Senator Leahy does provide a chart — unsupported by any citation to an authority of any kind — that expresses his opinion of what each claim is worth. See Committee Report p. 200.

their financial interest. Congress, therefore, bears a special responsibility to make the right decisions on the key issues discussed above — finality and award levels — in order to ensure that the trust fund is the permanent solution. If Congress fails in this regard and passes a flawed bill, the fund could indeed collapse. If that happens, and Congress must revisit the issue again several years from now, it will be doing so after having created effective floors on award amounts. Moreover, some will argue that Congress has created an "implicit federal backstop" for the fund, and that all claimants will have a right to receive the award amounts *even if private contributions are no longer available.* The future political environment could bind Congress's hands and force it to provide that money. This result would be the worst of all worlds — a flawed bill today that guarantees excessive awards that ultimately must be paid for by the taxpayers. Congress cannot let that happen; the way to prevent it is to ensure finality and reasonable awards.

Conclusion

There is no serious disagreement over whether a comprehensive national solution for asbestos victims and defendants is needed, but the FAIR Act cannot be that solution without two fundamental adjustments: a guarantee of finality, and reasonable award values that will not bankrupt the fund's contributors. Negotiations are continuing under the leadership of Chairman Hatch, but Democrats are demanding a prohibitively expensive fund, and time is running out this year. There are few challenges more important to our economy than resolving this issue so that asbestos litigation can be put behind us once and for all.

Staff Contact: Steven J. Duffield, 224-2946